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## BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

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IN THE MATTER OF THE GENERIC  
PROCEEDINGS CONCERNING ELECTRIC  
RESTRUCTURING ISSUES.

Docket No. E-00000A-02-0051

IN THE MATTER OF ARIZONA PUBLIC  
SERVICE COMPANY'S REQUEST FOR A  
VARIANCE OF CERTAIN REQUIREMENTS  
OF A.A.C. R14-2-1606.

Docket No. E-01345A-01-0822

IN THE MATTER OF THE GENERIC  
PROCEEDING CONCERNING THE  
ARIZONA INDEPENDENT SCHEDULING  
ADMINISTRATOR.

Docket No. E-00000A-01-0630

IN THE MATTER OF TUCSON ELECTRIC  
POWER COMPANY'S APPLICATION FOR A  
VARIANCE OF CERTAIN ELECTRIC  
COMPETITION RULES COMPLIANCE  
DATES.

Docket No. E-01933A-02-0069

IN THE MATTER OF THE APPLICATION  
OF TUCSON ELECTRIC POWER  
COMPANY FOR APPROVAL OF ITS  
STRANDED COST RECOVERY.

Docket No. E-01933A-98-0471

The Residential Utility Consumer Office ("RUCO") hereby provides notice of filing the  
Testimony Summaries of Marylee Diaz Cortez and Dr. Richard A. Rosen, in the above-  
referenced matter.

RESPECTFULLY SUBMITTED this 14th day of June, 2002.

  
Scott S. Wakefield  
Chief Counsel

1 AN ORIGINAL AND EIGHTEEN COPIES  
2 of the foregoing filed this 14th day  
3 of June, 2002 with:

3 Docket Control  
4 Arizona Corporation Commission  
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5 COPIES of the foregoing hand delivered  
6 this 14th day of June, 2002 to:

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## **SUMMARY OF MARYLEE DIAZ CORTEZ' TESTIMONY ON BEHALF OF RESIDENTIAL UTILITY CONSUMER OFFICE**

The Commission, in approving APS's stranded cost settlement, authorized APS to recover transition costs through an adjuster mechanism to commence on July 1, 2004. The ACC's authorization of the adjuster mechanism essentially serves as an accounting order, permitting APS to defer certain costs for future recovery. Thus, APS is currently creating an ever-growing liability to ratepayers for the cost of restructuring the industry. In effect, as we speak the "meter is ticking" on Arizona ratepayers future utility rates.

As long as the feasibility and desirability of electric competition remains in question, APS should not continue to be permitted to accrue an ever-mounding liability for the cost of transitioning to competition.

If the Commission is reluctant to rescind APS's deferral accounting order at this time, the Commission could add certain conditions to the order to protect ratepayers from the ever-mounting liability. The ACC could add the following conditions:

- 1) Any deferrals accrued subsequent to the order in this docket are not guaranteed recovery, and will be subject to audit and review in the next rate case;
- 2) Any deferrals accrued subsequent to the order in this docket, if allowed for recovery, will not necessarily be afforded rate base treatment (i.e. earn a return);
- 3) APS will bear the burden of proving the reasonableness, prudence, necessity, and ratepayer benefit from any costs deferred subsequent to the issuance of an order in this docket.

## **SUMMARY OF DR. RICHARD ROSEN's TESTIMONY ON BEHALF OF RESIDENTIAL UTILITY CONSUMER OFFICE**

After reviewing the direct and rebuttal testimony of all the witnesses in this case, I have come to the following conclusions and recommendations for the ACC:

1. The state and federal regulatory issues affecting electric industry restructuring are far more complex than most analysts and commissioners believed just a few years ago, when the ACC established electric restructuring regulations for Arizona.
2. The main lesson of the California and related state restructuring experiences is that the ACC should proceed slowly and cautiously if it decides to continue to pursue electric industry restructuring.
3. There are many analytical, legal, and regulatory studies that should be done for Arizona before electric industry restructuring or generation divestiture should proceed.
4. The Commission should not lose sight of the fact that continued study of electric deregulation, as I and Staff have recommended if the Commission wants to pursue divestiture, would result in additional costs to customers.
5. Almost every witness in this docket seems to agree that the restructuring process in Arizona, including divestiture, cannot possibly be completed by January 1, 2003, no matter what that process ends up consisting of. Therefore, at a minimum, the ACC should approve a variance to delay for at least one year the implementation of the Electric Competition Rules for all utilities in Arizona, in order to give the ACC time to properly handle these complex issues. However, it may even make more sense for the ACC to just suspend implementation of the Electric Competition Rules for between 3-5 years, in order to let the wholesale market mature. This might be the best course of action before

Arizona divests any existing generation into unregulated subsidiaries of existing electric utilities, which could harm ratepayers in the long run.

6. Almost every witness, except the APS witnesses, agrees that Arizona utilities will have the substantial ability to exercise market power in wholesale electric markets within Arizona, if all the existing generation assets of each utility are simply transferred to an unregulated affiliate of that utility. This would include monopoly-pricing power in certain Arizona load pockets near times of peak demand, but would also include market power during many other times of the year, as well. This would, of course, be unacceptable. The APS application of the new FERC SMA test for market power is critically flawed, as Mr. Roach points out, and the test itself is inadequate in principle anyway.
7. APS witness Dr. Hieronymus is correct that APS (or TEP) could not exercise market power with their existing generation assets in Arizona if that power were sold to Standard Offer customers on fixed-price basis under a long term PPA. Thus, a necessary condition for the ACC allowing divestiture to go forward is for all the output of existing generation assets to be made available to Standard Offer customers on a traditional cost-of-service basis for the duration of their operational lifetime, so that ratepayers can continue to receive the very substantial economic benefits of these generating units.
8. I support the Staff recommendation that before divestiture is allowed to occur, the ACC would have to perform a comprehensive market power study for the Arizona regional wholesale power market. However, contrary to Staff, I believe that the market power study should be performed on a cooperative basis with input from all parties through the creation by the ACC of a technical advisory committee. The results of this study should

be subject to review in a formal docket with expert testimony on how to interpret the results, and on the strengths and weaknesses of the study. This study must primarily consist of computer-based modeling of strategic behavior, including strategic bidding and capacity withholding. The methodology described in Appendix A of the 1996 FERC merger guidelines, as recommended by Staff, is not adequate.

9. The results of the recommended market power study should, then, be used by the ACC, and the other parties, to determine how and to what extent electric industry restructuring should continue to be pursued in Arizona.
10. However, given the evidence relevant to such an analysis of the potential for the exercise of market power in Arizona that has already been entered into the record in these dockets, I agree with Mr. Pignatelli of Tucson Electric that the ACC should completely re-evaluate the costs and benefits and the other pros and cons of trying to achieve competition in the electric power industry, and that this "should include a review of the basic premise that competition is in the public interest." (Direct, Page 17) I share Mr. Pignatelli's obvious skepticism that "competition" in this industry can ever be made to work in a way that would benefit any significant group of electricity ratepayers. Thus, in parallel with a market power study as recommended by Staff, I recommend that the ACC do what Mr. Pignatelli urges in his direct testimony, namely to require "proponents of electric competition to come forward with credible evidence of the anticipated benefits of electric competition ...to affirm or reject what seems to be the presumption that Electric Competition is the best manner for providing electric service in Arizona." (Page 18) A second set of hearings should be used for this purpose prior to proceeding with generation divestiture.

11. Contrary to Mr. Roach's belief, FERC issues are highly relevant to this docket. Given FERC's relatively poor track record to-date of monitoring and mitigating market power in US wholesale electric markets, I do not believe that the ACC should assume that FERC will do an adequate job of protecting Arizona consumers from the negative impacts of wholesale market power on retail rates. Furthermore, the Standard Market Design that FERC staff has proposed for all RTOs is highly problematic, and the ACC should not allow Arizona utilities to participate in an RTO until the net benefits of such an institution to Arizona are clearly demonstrated.
12. Mr. Pignatelli's recommendation that only customers with loads of 3 MW or greater be allowed to participate in retail competition within Arizona is a reasonable option for the ACC to consider, *if* traditional cost-of-service bundled retail rates are maintained for all other customers, and if divestiture is not carried out.
13. Any competitive bidding process for generation that is used in Arizona should be based on least-cost planning principles, and should integrate planning for demand-side management technologies as well as new transmission system investments, with bidding for generation. The ACC should, in any event, set a required planning reserve margin for each utility distribution company that it regulates within Arizona, in order to ensure the continuation of adequate electric system reliability.